
# PLEXUS Market Comments

Market Comments – September 19, 2019

NY futures retreated this week, as December dropped 188 points to close at 60.33 cents/lb.

Last week's 500-point jump from a low of 58.23 to a high of 63.39 cents proved to be nothing more than a technically induced short-covering rally. Trade selling became quite heavy once prices moved above 62 cents, which eventually stopped the market in its tracks and forced it to pull back.

The fact that overall open interest went up slightly during the market's advance seems to confirm that it was indeed a handover of specs shorts to the trade, and possibly some new spec buying into new trade selling. It will be interesting to see what changes the CFTC report is going to show tomorrow.

US export sales remained tepid last week, as net sales amounted to just 120,200 running bales of Upland and Pima cotton for both marketing years. Once again we saw substantial cancellations totalling 57,700 running bales, of which 39,300 bales came from China. Shipments were quite slow as well at 173,800 running bales.

Total commitments for the season are now at 8.8 million statistical bales, of which a little over 1.5 million bales have so far been exported. For next marketing year sales are so far at a little over 0.7 million statistical bales.

The US cotton belt has experienced some unseasonably hot and dry conditions lately, with mixed results for the crop. While it has helped to get some fields ready for harvest, it seems to have taken a toll on some late maturing cotton. The US crop is still a moving target in regards to size and quality and this is one of the reasons why we don’t think the trade is going to chase prices too much lower from here.

Another reason for the shorts to be cautious is a potential resolution to the US/China trade conflict in early October. Both sides have shown some goodwill recently, raising hopes that a compromise in certain areas of the dispute might be reached. We don’t think that we are going to see a comprehensive trade deal anytime soon, but what if Ag imports were to open up, which is something that would benefit both countries?

China’s Reserve will have auctioned off another 1.0 million tons by the end of this month, which leaves it with less than two million tons. Most observers feel that 1.5 million tons will be the low-water mark, which would imply that sooner or later we will see the Reserve back as a buyer. A trade deal on Ag imports combined with cheap US cotton prices is therefore something the shorts need to keep an eye on.

On the monetary front we had another drop in interest rates by the Fed this week, as well as an emergency injection of over USD 75 billion after overnight rates briefly spiked to 10 percent due to a liquidity crunch among banks. It is unclear whether this was just a fluke or whether it was the first sign of stress in the system.

However, what seems clear is that markets demand more cheap money and that central bankers around the globe are willing to oblige. We therefore believe that inflation will sooner or later stage a comeback and that running short positions in such an environment becomes a risky proposition. A slowing economy combined with accelerated money printing could ultimately lead to 'stagflation', which means that nominal prices would rise even if the economy were to head into recession.

**So where do we go from here?**

Last week's rally looks like a flash in the pan on the chart and the market has now fallen back to the 6025 breakout level. However, the low volume over the last couple of sessions suggests that it was more a lack of buying than heavy trade selling that caused the market to recede.

Markets often retest support and resistance after a breakout and this could be the case here. If the market were to hold above 60 cents, we might see another wave of spec short covering that lifts the market back into the low-to-mid 60's, where overhead trade selling is waiting. With all the uncertainties currently hanging over the market we simply don't see speculators or the trade becoming aggressive sellers below 60 cents.

From a fundamental point of view we need to consider that even though ROW ending stocks are projected to reach around 50 million bales by the end of the season, 12 million of those bales are in India and carry a much higher price tag. In other words, apart from Brazil and WAF there aren't that many other attractive choices, which is why we believe that US prices don't need to get any cheaper at this point.

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